

RD AN No. 3598 (1930-C)  
December 12, 2000

TO: State Directors  
Rural Development

ATTENTION: MFH Program Directors/Managers

FROM: James C. Kearney  
Administrator  
Rural Housing Service

SUBJECT: Maintaining Acceptable MFH Project Management  
with Effective Servicing Actions

PURPOSE:

This Administrative Notice (AN) is issued to provide examples of requirements for determining acceptable management and implement streamlined servicing guidelines in individual Multi-Family Housing (MFH) projects.

COMPARISON WITH PREVIOUS ANs:

This AN reissues RD AN No. 3511(1930-C) issued January 20, 2000.

BACKGROUND:

RD Instruction 1930-C provides guidance in managing and operating MFH projects. RD Instruction 1965-B provides guidance in servicing MFH projects. Many states have or are in the process of developing standards for evaluating management performance.

This AN provides examples of requirements that states should use in determining acceptable management, issuance of Servicing Guide Letters or contacting borrowers to notify them of defaults in meeting their loan obligations, borrower responsibility in proposing corrective actions and definition of adverse actions related to servicing actions requiring appeal rights or review rights.

IMPLEMENTATION:

Project management criteria should be reviewed by the servicing official annually as part of the overall annual analysis or when critical problems in operational management become apparent through supervisory visits, physical inspections or compliance reviews.

EXPIRATION DATE: December 31, 2001

FILING INSTRUCTIONS:  
Preceding RD  
Instruction 1930-C

The following requirements are examples of what project management must provide evidence of in order to be considered as acceptable MFH management.

1. Current approved management plans or agreements.
2. Current approved operating budgets.
3. Current acceptable annual financial statements or audits.
4. Property is adequately maintained to secure the loan.
5. No outstanding health and safety violations.
6. No findings of civil rights or Fair Housing Act violations.
7. No outstanding record of misappropriated funds, including tenant subsidies.
8. Property taxes current.
9. Maintenance of adequate property insurance and fidelity coverage.
10. No outstanding suspensions, debarments or voluntary exclusions from program participation on the part of the management company or its principals.
11. No unidentified Identity of Interest relationships between the management company or its principals and the borrower, service providers, suppliers, or others involved with the ownership or operation of the MFH property.

All of the above are currently required by either Rural Housing Service (RHS) regulations, the loan agreement, promissory note or mortgage. When a borrower receives a loan, they have agreed to meet these requirements as a condition of loan approval. If deficiencies in any of the above are noted, project management is not considered acceptable. There may also be other serious management deficiencies related to operating practices noted in a supervisory visit report or during a physical inspection which should also trigger the use of the servicing guide letters attached.

All servicing Guide Letters are to be sent to the borrower with a copy to the management agent. It is the borrower's responsibility to provide acceptable management in MFH projects. It is also the borrower's responsibility to propose corrective actions once they have been notified of defaults.

It is Rural Development's responsibility to notify the borrower as soon as defaults are noted, review proposals for corrective actions submitted by the borrower, and determine whether these proposals will adequately solve the problems. If the proposals are acceptable, the servicing official should enter into a formal workout plan with the borrower, as the responsible party, and not the management company.

#### USE OF WORKOUT PLANS AND PROTECTIVE ADVANCES:

Approval of a workout plan as a servicing tool is not guaranteed to the borrower in any loan instrument or RHS regulations. Workout plans are not a form of loan assistance but are a tool Rural Development should use to cooperatively work with the borrower to effectively resolve defaults if the borrower is acting in good faith to actively propose realistic corrective actions.

Protective advances are not a form of loan assistance to the borrower, but are to be used to protect the Government's interest in the property in emergency situations when the borrower has not met their loan obligations or the tenants' health and safety may be affected if action is not taken immediately. Legal authorization for use of protective advances is described in the real estate mortgage and RD Instruction 1955-B. Issuance of appeal rights is not applicable to protective advances.

### USE OF SERVICING GUIDE LETTERS:

Rural Development should use the servicing Guide Letters to notify the borrower of deficiencies. It is the borrower's responsibility to submit a proposal to correct deficiencies if they choose to do so, rather than Rural Development's responsibility to make demands of the borrower. Rural Development should not require that the borrower change management or repay unauthorized assistance, but should notify the borrower of all defaults. Change of management or repayment of unauthorized assistance may be criteria for determining if a workout plan is acceptable and approved by Rural Development. Failure to offer to change management or repay unauthorized assistance may result in rejection of a proposed workout plan.

Guide Letter, Attachment A, gives the borrower 15 days to contact the servicing official with a proposal to correct deficiencies either immediately or with a workout plan. Guide Letters, Attachments B and C should be sent to the borrower and management company when deficiencies are not resolved with the borrower in a timely manner. When the borrower does not correct deficiencies in response to the initial Guide Letter, Attachment A, and the subsequent servicing letters are used, the borrower will be considered in default of their loan obligation.

Defaults and deficiencies in workout plan proposals should be detailed specifically in all servicing Guide Letters so that the borrower has notice of failure to meet their loan obligations, and the opportunity to submit a plan for correction within the timeframes outlined.

If the borrower enters into a workout agreement and later defaults on that agreement, the servicing official should continue with the next servicing action. In some circumstances, workout agreements may be renegotiated if the servicing official determines conditions beyond the borrower's control caused the default. Workout agreements should not be renegotiated just to bring the borrower into compliance in order to become eligible for additional loans.

If it is necessary to send Guide Letter Attachment C or accelerate the account, copies of these notices must also be sent to any known limited partners or syndicators with an interest in the project so that they are notified of defaults to loan obligations that could affect their interest in the project.

### ISSUANCE OF APPEAL RIGHTS OR REVIEW RIGHTS:

Rural Development may find it necessary to prepare a problem case report to initiate acceleration of the account if: (1) the borrower does not respond, (2) defaults are not corrected, or (3) a mutually acceptable workout plan or alternative servicing action such as a transfer, change of project management or ownership cannot be approved. All workout plans or alternate servicing actions must be in the best interest of the Government and tenants and developed in a reasonable timeframe.

The acceleration of the account is an adverse action that does require the borrower be given appeal rights. Demands for repayment of unauthorized assistance should be made as part of the acceleration action and included with proper reference in the acceleration letter. Involuntary change of management should be pursued through a request for a court appointed receiver to manage the property through the liquidation process. This will make it necessary to only issue appeal rights once and hold one appeal for all issues.

If it is necessary to initiate acceleration of any loan account, servicing officials should ensure adequate documentation of the conditions affecting the property is in the file. This documentation should include pictures, tenant interviews and a trend analysis documenting financial discrepancies. After the appeal process is concluded, this documentation will be necessary to pursue legal action to request a court appointed receiver to manage the property through the foreclosure process.

If a project is receiving tax credits through a state agency, that agency should be notified of non-compliance with loan obligations after the appeal process is concluded and the loan is forwarded to your Office of the General Counsel Office (OGC) for continued foreclosure action.

Acceleration of accounts can be initiated without using the specified Guide Letters if sufficient and appropriate documented servicing has already taken place or the type of default warrants immediate action. If you have any questions concerning the sufficiency of prior servicing, please contact OGC for an opinion.

#### IMPROVEMENT OF 515 MANAGEMENT:

Timely and effective servicing must be implemented before projects and management deteriorates to an unacceptable level. This will give the borrower the opportunity to take corrective actions before significant financial losses are incurred and physical deterioration of the property jeopardizes the health and safety of the tenants or the security value of the project.

We recognize that most of the projects in the 515 portfolio are well managed and are operating in compliance. Our goal is to encourage good management that will improve the physical condition of 515 projects, maintain the security value of each project, and provide the service the tenants are entitled to receive.

Questions regarding this AN should be directed to James E. Vollmer, Multi-Family Housing Portfolio Management Division at 202-720-1060.

Attachments

ROUTINE NOTICE OF SERVICING RESULTS/CONCERNS

\_\_\_\_\_  
Date

Dear \_\_\_\_\_:

We are writing to inform you of the results of a recent review of certain selected aspects of your operations. A copy of the results of our review is attached [Attach copy of supervisory visit report, physical inspection report, compliance review, reserve records, notice of payment due, etc.].

Please review the attached material and note the areas of concern listed. [We want to especially bring to your attention the following items:]

We are asking that you contact this office within 15 days of the date of this letter to inform us of the corrective actions you have taken, or plan to take, to correct the concerns listed.

Our office address and telephone number are: [insert address and telephone number]

Sincerely,

\_\_\_\_\_  
(Signature and title of Official)

Attachment

NOTIFICATION OF SERIOUS SERVICING CONCERNS

\_\_\_\_\_  
Date

Dear \_\_\_\_\_:

We are writing to inform you that certain aspects of your project operations are of serious concern to the Agency.

A brief description of the items of concern which warrant attention is [provided below:] [attached.]

We would like to arrange a meeting to discuss these concerns. [Please contact our office to confirm if you can make the tentatively scheduled meeting at the following time, date, and location:] OR [Please contact our office within 15 days of the date of this letter to make the necessary arrangements]. Our address and telephone number are (insert address and telephone number).

Please be prepared to discuss the matters of concern identified. [In particular, you may want to bring the following information to the meeting:]

We look forward to hearing from you.

Sincerely,

\_\_\_\_\_  
(Signature and title of Official)

Attachment

NOTIFICATION OF INTENT TO PURSUE  
MORE FORCEFUL SERVICING ACTIONS

\_\_\_\_\_  
Date

Dear \_\_\_\_\_:

We regret that earlier attempts to resolve [state the problems] have not been successful.

We are writing to inform you that Rural Development intends to take further action unless alternative arrangements are promptly made with this office. If you have not contacted us within 15 days, we intend to pursue the [following actions:] [attached actions.]

[List actions, e.g., Forward a problem case report to the State Director, recommend an investigation by the Office of the Inspector General, demand a change in project management, place a recoverable cost charge on the account, forward a recommendation to the State Director to issue a Notice of Acceleration, etc.]

We are hopeful we can avoid the necessity of taking the steps outlined above. Unfortunately, we will be forced to do so unless we hear from you within 15 days from the date of this letter. Please contact our office immediately if you wish to avoid the actions described above.

Sincerely,

\_\_\_\_\_  
(Signature and title of official)

[Attachment(s)]

LIST OF SERVICING OPTIONS AVAILABLE UNDER RHS INSTRUCTIONS  
FOR USE IN BORROWER SERVICING MEETINGS

1. Special servicing or workout plan. Servicing or workout plans may include consideration of RHS approved marketing incentives, rent changes, Special Market Rent levels, and other actions set out in Exhibit F of RD Instruction 1965-B (available upon request).
2. Reamortization (see RD Instruction 1965-B). Reamortization actions are normally approved at the end of a successful servicing or workout plan in order to achieve long-term financial viability. Reamortization actions should not be approved solely to remove a delinquency.
3. Substitution of key owners, partners, and managers, changes in management agents, subordination, consent to incur additional non-trade debt, and other miscellaneous servicing actions set out in RD Instruction 1965-B.
4. Transfer to eligible applicant (see RD Instruction 1965-B).
  - a. Same terms.
  - b. New terms.
    - (1) Transfer full indebtedness.
    - (2) Transfer for less than the debt and process a subsequent debt settlement action.
5. Transfer to an ineligible applicant (see RD Instruction 1965-B).
6. Voluntary conveyance to the Government (see RD Instruction 1955-A).
7. Early payment of the loan (see RD Instruction 1965-E).
8. Payment application information and late fee waivers (see RD Instruction 1951-K).
9. Adverse servicing actions. Should it not be possible to mutually resolve issues of concern, the Agency may find it necessary to pursue one of the following servicing actions:
  - a. Issuance of a problem case report and a notice to owners of record of RHS's intent to accelerate if problems cannot be satisfactorily resolved within timely manner (see RD Instruction 1955-A).
  - b. When recovery efforts are warranted due to suspected unauthorized assistance which is not possible to be mutually resolved, issuance of a demand for recovery of unauthorized assistance (see RD Instruction 1951-N).
  - c. When serious failure to uphold responsibilities are evidenced, issuance of a suspension or debarment notice (see RD Instruction 1940-M).